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Via Electronic Mail

Secretariat to the Financial Stability Board  
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**Re: Financial resources to support CCP resolution and the treatment of CCP equity in resolution**

Ladies and Gentlemen:

The Depository Trust & Clearing Corporation (“DTCC”) welcomes the opportunity to comment on the Consultative Document prepared by the Financial Stability Board (“FSB”) entitled ***Financial resources to support CCP resolution and the treatment of CCP equity in resolution*** (“Discussion Paper”).<sup>1</sup> We also appreciate the active engagement of the FSB in the ongoing discussions among regulators, clearinghouses (“CCPs”) and industry groups on this topic, and hope that our views will be taken into consideration in preparing the next stage of proposed resolution guidance for CCPs. The Discussion Paper poses a series of questions grouped around specific themes and issues. Our response addresses these issues thematically.

**Introduction**

DTCC is the parent company and operator of the U.S. cash market securities CCPs, National Securities Clearing Corporation (“NSCC”) and Fixed Income Clearing Corporation (“FICC”), both of which have been designated as systemically important financial market utilities (“SIFMUs”) by the U.S. Financial Stability Oversight Council (“FSOC”) pursuant to Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank”). NSCC and FICC provide critical clearing and settlement services for multiple asset classes, including US equities, corporate and municipal bonds, and government and mortgage-backed securities. NSCC and FICC are registered under the Securities Exchange Act of 1934, as amended, as clearing agencies, are supervised by the U.S. Securities and Exchange Commission (“SEC”),<sup>2</sup> and have comprehensive recovery and wind-down plans that have been approved by the SEC.

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<sup>1</sup> See FSB, Discussion Paper (Nov. 15, 2018), available at <http://www.fsb.org/wp-content/uploads/P151118-2.pdf>.

<sup>2</sup> DTCC is also the parent company of The Depository Trust Company (“DTC”), the U.S. central securities depository. Like NSCC and FICC, DTC is designated as a SIFMU, is a registered clearing agency supervised by the SEC and its recovery and wind-down plans were approved by the SEC. In addition, as a New York Limited Purpose Trust Company

DTCC is owned and governed by the users of its SIFMU subsidiaries, all of whom commit capital as owners, pay fees for services and ultimately benefit from the safeguards, efficiencies and risk mitigation that DTCC provides.

## **General**

The Discussion Paper follows on from the FSB Guidance on Central Counterparty Resolution and Resolution Planning (“FSB Guidance”)<sup>3</sup> to assist authorities in their resolution planning for CCPs, and from the FSB’s commitment to continue further work on financial resources to support CCP resolution and on the treatment of CCP equity in resolution. While DTCC agrees much work has been done to develop a framework for financial market infrastructure resolution, the actual resolution strategies and planning for certain CCPs by the Resolution Authorities we understand are still in development in many respects. We believe that further work providing transparency into the Resolution Authorities’ decision-making underpinning its approach to CCPs is both necessary and advisable to provide greater clarity to both CCPs and their participants. Greater transparency will enable CCPs and their participants to further evaluate the issues raised in this Discussion Paper.

Specifically, we offer the following comments for the FSB’s consideration:

### **Assessing the adequacy of financial resources to support resolution**

The Discussion Paper proposes a five-step process to assess the adequacy of financial resources that a CCP has to support resolution. These are, briefly, as follows:

1. identifying hypothetical default and non-default loss resolution scenarios;
2. evaluating existing tools and resources available for resolution;
3. analyzing the full resolution costs;
4. comparing existing tools and resources to resolution costs, so as to identify any gaps; and
5. considering the availability, and the attendant costs and benefits, of potential means to address any identified gaps.

The paper provides a discussion of these steps and categories of scenarios and tools, broadly within the context of default-related losses and non-default losses.

We believe that this approach could provide relevant authorities a useful and logical framework within which to analyze available financial resources, as they develop their resolution approaches for CCPs. Concomitantly, this approach requires an individualized analysis for each CCP within a Resolution Authority’s jurisdiction. This would require the Resolution Authority, particularly if it is not the CCP’s supervisory or prudential authority, to be familiar with the CCP’s ownership, capital structure, products, rules, and recovery and wind-down plans in order to maintain a resolution approach (in close

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and state member bank of the Federal Reserve System DTC is subject to supervision and examination by the New York State Department of Financial Services and the Federal Reserve Bank of New York under delegated authority from the Federal Reserve.

<sup>3</sup> See FSB, Guidance on CCP Resolution and Resolution Planning (July 5, 2017), *available at* <http://www.fsb.org/wp-content/uploads/P050717-1.pdf>.

coordination with the CCP's supervisory authorities) best suited for that entity. We think this is appropriate—and necessary—to ensure that the Resolution Authority does not apply a “one size fits all” approach with unintended consequences. It is equally important that such a framework not be used as a mechanism to substitute the Resolution Authority's views for that of the Supervisory Authority with respect to decisions or determinations necessary to assess a CCP's compliance with the relevant regulatory framework.

In this regard, we support the FSB's view that the nature and specific features of a particular CCP and the products it clears “may affect the design of a resolution strategy and resolution plan.”<sup>4</sup> However, this is true not only with the respect to the type of products that a CCP clears, but also the ownership and governance structure of a CCP, which should be carefully and separately considered for these purposes.<sup>5</sup> Such an analysis is important to better understand the relevant alignment of incentives with respect to a CCP's resiliency, as well as the potential costs and benefits associated with any potential measures that could be adopted to address potential gaps between existing tools and resources and resolution costs.

In addition, when considering CCP resolution planning, DTCC agrees that regulators and resolution authorities should understand the types of events that could push CCPs to the point of resolution. However, we believe that this is only likely to result from extreme events that even under hypothetical non-default loss scenarios, will most likely involve the simultaneous default of multiple global systemically important bank (“GSIB”) participants. As such, the highly unlikely nature of a resolution event mandates that regulators apply a careful risk reward analysis when deciding appropriate capital and replenishment approaches for CCP resolution frameworks. The benefits of prefunding a separate pool of capital to be available only to Resolution Authorities must be realistically assessed against the costs that would impose on centralized clearing, particularly for smaller participants. This may result in further concentration of CCP membership, which increases the potential for systemic risk. Rather, we think a better result would be for Resolution Authorities to work with the CCPs and their primary regulators on measures taken to address capital needs in the event of a wind-down or resolution, so as to facilitate the development of creative responses which are CCP-led and customized to the relevant market and structure, rather than mandated by resolution authorities.

### **Treatment of CCP equity in resolution**

The second half of the Discussion Paper is devoted to a discussion of the treatment of CCP equity in resolution. At a high level, the concern that the FSB is attempting to address is whether in CCP models the application of their rules-based waterfall would result in protecting equity-holders in a manner that is somehow unfair to the CCP's users. The drafters note that in applying the “No creditor worse off in Liquidation” counterfactual, you have to assume that in liquidation the rules-based waterfall would (and it is appropriate to) be followed in full. The Discussion Paper then goes on to discuss various approaches to recapitalizing CCPs in resolution, including the possibility of writing down equity and bailing in debt as a means to achieve this.

While DTCC does believe that resolution authorities should be able to write down or bail-in equity or unsecured debt in a manner that respects the insolvency claims hierarchy (but does not disincentivize or interfere with the provision of credit or liquidity to the CCP), we do not believe that any mandated TLAC-type requirement is appropriate for CCPs. Regulators should be wary of applying a GSIB recovery tool

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<sup>4</sup> Discussion Paper at 4.

<sup>5</sup> While the Discussion Paper asks whether “the assessment of financial resources for CCP resolution take into account... different CCP ownership structures”, it does not include an analysis of the potential impact different CCP ownership structures could have on each of the steps within the proposed framework.

to CCPs, whose business model, risk profile capital structure, and loss-absorption approach are very different. Though the concept of bail-in may have an enticing simplicity, Resolution Authorities need to avoid conflating the types of debt and equity, and the purposes they serve, maintained by banks, with that of CCPs. Unlike banks, CCPs are more monoline businesses and have predefined and predictable loss mutualization. Requiring them to hold substantial prefunded cash resources beyond existing regulatory requirements<sup>6</sup> risks making CCP's de-facto investment companies which, in and of itself, would introduce a whole new set of investment and custody risks. Such overcapitalization could also displace the supervisory authority's judgement regarding the sufficiency of a CCP's resources to serve as an effective risk management device for relevant market participants and promote continuity of access in the event of a large scale market disruption. Moreover, we do not believe this is the best use of industry resources, and could serve to further concentrate CCP membership (and have implications for the amount of capital that participants themselves must hold) and also impede access to diverse sources of liquidity for the CCP in times of stress. Further, as discussed above, we believe that more effective responses to a potential wind-down or resolution event could be developed where the Resolution Authorities, CCPs, and their primary regulators work together. Accordingly, given these possibilities and the burden that could be placed on CCPs' diverse memberships, we do not support reserving any funds solely for resolution.<sup>7</sup> In other words, it should be the "presence of the authority that distinguishes resolution,"<sup>8</sup> not whether any tools or resources are reserved for use in resolution.

We further note that the development of additional guidance with respect to the treatment of CCP equity in resolution would "have to take into account the ownership structure of the CCP."<sup>9</sup> As mentioned above, DTCC is a user owned and governed utility. The DTCC common shareholders include hundreds of banks, broker dealers, and other companies in the financial services industry that are participants of one or more of DTCC's SIFMU subsidiaries, and the DTCC board is currently composed of 19 participant and non-participant directors. Importantly, our ownership structure also ensures that we direct our primary focus toward addressing industry needs and preserving market stability, which is especially critical during times of crisis. This ownership model effectively aligns interests among our users (who are also our owners), our board of directors and management particularly with respect to participant access and maintaining continuity of service of the SIFMU businesses. Accordingly requiring a user-owned CCP to set aside financial resources for resolution through the use of a debt instrument such as TLAC would disrupt this alignment of interests.

Additionally, when considering the treatment of a CCP's equity in resolution, it is important to evaluate how the insolvency rules would affect the operational continuity of CCPs with a variety of types of ownership and governance structures. For example, losses assessed against 'owners' may have a different effect on a CCP owned by its participants (such as the DTCC CCPs) compared to a CCP owned as a public stock company. In the former ownership structure, members will be absorbing losses

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<sup>6</sup> See 17 CFR 17Ad-22(e)(4), 17 CFR 17Ad-22(e)(7), and 17 CFR 17Ad-22(e)(15). See also Principles 4, 7, and 15 of the Committee on Payment and Settlement Systems and Technical Committee of the International Organization of Securities Commissions ("CPSS-IOSCO"), Principles for financial market infrastructures (Apr. 16, 2012), available at <http://www.bis.org/publ/cpss101a.pdf>; and Standards for Covered Clearing Agencies, Exchange Act Release No. 34-78961, 81 Fed. Reg. 70786 (Oct. 13, 2016).

<sup>7</sup> In addition, as we've stated previously, we believe that no tools (whether VMGH, partial tear-ups, cash calls or otherwise) should be reserved solely for resolution authorities that could not also be used by CCPs themselves, if they are appropriately included ex ante in CCP rulebooks. See, e.g., DTCC Letter to the FSB Discussion Note regarding Essential Aspects of CCP Resolution Planning (Oct. 17, 2016), available at <http://www.fsb.org/wp-content/uploads/Depository-Trust-Clearing-Corporation.pdf>.

<sup>8</sup> A CCP is a CCP is a CCP, Robert T. Cox and Robert S. Steigerwald, Federal Reserve Bank of Chicago Working Paper, 14 (April 2017), available at <https://www.chicagofed.org/~media/publications/policy-discussion-papers/2017/pdp-2017-01-pdf.pdf>.

<sup>9</sup> Discussion Paper at 21.

in their roles as participants as well as in their roles as owners, and this may affect their willingness and ability to carry on as part of the CCP and, by extension, the resiliency of the CCP. For these reasons, we strongly believe that the FSB should not mandate the provision of equity to CCP participants under any particular set of circumstances. Such issues are better addressed with within the purview of the CCP, its supervisory authorities, and participants.

**Transparency**

While much work has been done and published setting forth the resolution framework for GSIBs, the resolution framework for CCPs is neither fully developed in certain jurisdictions, nor is it transparent to the CCP or its participants. Transparency is critical to ensure continued trust in the system, which is vital for CCPs to be able to continue providing its services through its recovery process as well as through a potential resolution. Resolution Authorities should clearly articulate both the choices they make/plan to make for a CCP's resolution strategy, and the reasons for the choices they make.

In addition, while the Discussion Paper identifies several scenarios where resolution may be called for, it is unclear how such determinations should be made particularly in jurisdictions where a CCP's supervisory authority and Resolution Authority differ. For example, the Discussion Paper states that resolution may be called for where the CCP does not meet existing CPMI-IOSCO standards, or does not have sufficient financial resources to cover non-default losses. The supervisory authority's role in making these determinations is unclear. It is important that where the resolution authority is not the CCP's supervisory authority, the Resolution Authority's decisions should be made in close consultation with the CCP's supervisory authority. For resolution to be successful, it is essential for the supervisory authority in the CCP's home country to play a key role in any decisions concerning a CCP's resolution. Legal authorities and methods can vary widely across jurisdictions, and the CCP's supervisory authority is likely to be in the best position to assess which resolution actions are most appropriate. Greater transparency surrounding the resolution regime for CCPs should help facilitate these discussions and provide regulatory and market participants with a greater understanding of their respective roles and obligations in a CCP resolution.+

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DTCC appreciates the opportunity to respond to the issues raised in the Discussion Paper and your consideration of the views expressed in this letter. We would welcome the opportunity to provide further detail on any of the matters discussed herein. If you have any questions or need further information, please contact me at [mpozmanter@dtcc.com](mailto:mpozmanter@dtcc.com).

Sincerely,



Murray Pozmanter

